Cash Management

Hutton case spurs corporate reviews

By Richard J. Gillespie

NEW YORK — Concerns that corporations might be open to charges that they are abusing their banks are surfacing in the wake of the E.F. Hutton case cash management consultants say.

Often it is the players at the top of the corporate hierarchy — chairmen, presidents and chief financial officers — who have asked cash and treasury management consultants to review their cash management operating procedures to get some kind of seal of approval, industry sources say.

A major issue for consultants in the wake of the E.F. Hutton revelations is that overdrafting, which is standard operating procedure at many corporations, has now come to be seen in a different light.

The circumstances under which corporate overdrafting practices have come to be challenged also are unsettling to many industry commentators, who believe it constitutes a bad precedent.

Bernell Stone, Mills B. Lane professor of banking and finance at Georgia Institute of Technology, has been supervising an investigation of laws governing these practices. So far, he reports they seem to be "unequipped to deal with today's modern practices."

Most recent cases were settled out of court, he said. As a result, there are few precedents that can be cited successfully.

What is illegal, he said, is for a corporation to create a circular path for transferring funds whose only purpose is to generate float, which E.F. Hutton appeared to have done, he said.

The problem with using the Hutton case as a precedent, he said, is that the brokerage firm clearly had violated a Securities and Exchange Commission regulation governing remote disbursing, and with the prospect of having its license revoked by the SEC, it chose instead to admit its guilt on other charges.

Mr. Stone believes E.F. Hutton might otherwise successfully have challenged the Justice Department on its overdrafting practice, he said.

"I suggest that if it had gone to court, it is not clear that they would have been found guilty," he said, echoing comments by other experts.

Furthermore, he said that had the Justice Department chosen to prosecute an industrial company, as opposed to a brokerage firm, for systematic bank overdrafting, it is not clear the department would have had any success, for the same reason.

"I think the most important thing is that there is a need to clarify the laws, and what is and is not an acceptable practice in terms of disbursing and concentrating funds," he said.

John Leahy, author of the California-based industry newsletter The Leahy Report, put in calls to legal authorities seeking some clarification on the issues, but no calls were returned, he said.

Calls by this publication to the Justice Department also were not returned.

There is, according to Mr. Leahy, a mail fraud statute and a wire fraud statute that might be construed as prohibiting intentional overdrafting, but he said the laws were so broad the Justice Department "could do something to almost anybody who has a gleam in his eye, and that sometimes it was justified and it was not," he said.

"If this thing goes all the way, the Justice Department is setting up a case law for cash management professionals and I think it is a bad case on which to base a precedent," Mr. Leahy said.

"They are taking the position that it is illegal to overdraw an account. I have had companies call and say they are overdrawing their accounts, and saying that the banks know about it and are being compensated for it.

"But questions are being raised and it is not an uncommon practice for corporations to do it with the knowledge of the banks."

Andrea Bierce, a cash management consultant with Peat Marwick Mitchell & Co.'s New York office, said she found there was a general concern among senior corporate executives who wanted confirmation that their companies were not doing anything that might be construed as illegal or unethical.

"The companies that are calling are saying, 'Do not tell anybody you are working with us.' There is a robe of secrecy that shows companies are concerned," said Ms. Bierce.

In Boston, Robert T. Mayer, manager of cash and treasury management consulting for Coopers & Lybrand, said he also had received inquiries.

"The way I perceive it, and the way people have responded to it, is that there is concern that like E.F. Hutton, they have overstepped the bounds," he said.

"What is interesting to me is that the media have not been as definite as they might, particularly in view of the fact that some of E.F. Hutton's branch offices were measured on a performance basis by the amount of interest they generated. So, effectively, some of their management systems drove them to this thing."

According to another source, a major defense contractor inadvertently exploited its banks through systematic overdrafting.

It came about, he said, because of the way an internal management system calculated the return on assets of its operating divisions. It became advantageous for field officers to reduce their cash balances as much as possible and as a result, they consistently overdrafted their banks and remitted funds to the cash control center. As a result of the lower cash balances reported in the internal accounting system, they boosted their return on assets significantly, he said.

Similarly in the Hutton case, Mr. Mayer said clearly there were banks in its fold that could have been eliminated, but he said they

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Payden & Rygel index of short maturities assets*
(for month ending June 30, 1985)

	Quarter Ending 3/31/85	June 1985	Quarter to date	Year to date	Yield level monthly change*
	Annualized total returns				
90 Day					
U.S. Treasury Bill	8.24	8.01	9.07	8.74	−32
Domestic C.D.	8.26	7.56	9.20	8.83	0
Euro $ C.D.	8.39	7.61	9.38	8.98	+5
180 Day					
U.S. Treasury Bill	8.28	9.04	11.39	9.95	−30
Domestic C.D.	7.82	7.56	10.91	9.47	0
Euro $ C.D.	8.22	7.71	11.17	9.81	0
1 Year					
U.S. Treasury Note	8.35	10.69	11.48	11.90	−27
2 Year					
U.S. Treasury Note	7.30	13.99	22.23	14.97	−25

*Figures are annualized total returns. Quarter-to-date and Year-to-date figures linked monthly. 90 and 180 Day Treasury Bill yield level changes on discount basis.
*Basis points.

Source: Payden & Rygel, Los Angeles, California 90017

Cost savings touted

CACHA calls move a boon

By Richard J. Gillespie

NEW YORK — A new era in electronic payments was ushered in this summer when the California Automated Clearing House Association switched its processing services from the Federal Reserve to General Electric Information Services Co.

Among the benefits to corporations in switching the electronic payment network to the private processor, which is a subsidiary of General Electric Co., are lower electronic payments costs, improved direct deposit capabilities, and later cutoff times for cash concentration, said Dave Kvederis, chairman of CACHA.

"The biggest benefit, clearly, will be the cost savings," said Mr. Kvederis, who is also senior vice president of Wells Fargo Bank.

"The Federal Reserve charges are anywhere from two to five times more than the private sector to process the same transaction."

The most spectacular example of cost savings, he said, is in the night-cycle transaction, which is a transaction for next-day settlement that goes through after the Federal Reserve's daily cutoff times, as most corporate cash concentration transaction debits do.

The Federal Reserve charges 6 cents for a night-cycle transaction, while CACHA will pay GEISCO only 1 cent, the same as it pays GEISCO for any type of transaction.

"There will be no night-cycle premium charged under the CACHA environment," he said.

The Federal Reserve charges CACHA 1.8 cents for each side of a two-day availability transaction, such as a direct deposit payment, that flows between San Francisco and Los Angeles. GEISCO again charges 1 cent.

The cost of a typical transaction goes from 3.6 cents under the Federal Reserve to 2 cents with the private sector.

"So for the large-volume financial institution, the cost saving is pretty significant on a per-transaction basis even without other savings," he said.

Other savings for financial institutions, which Mr. Kvederis said would be passed along to corporate customers, are in the elimination of the Federal Reserve's tape handling charge for every tape that is

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Testing plan met with ambivalence

By Fred Williams

The soon-to-be-unveiled professional certification program for cash managers might be headed for trouble, with some regional cash management association officials calling certification a waste of time and unnecessary.

A check by *Pensions & Investment Age* of several regional association spokesmen failed to turn up a single unqualified supporter of the program. Most were either ambivalent or openly critical of certification of cash managers as proposed by the National Corporate Cash Management Association.

The NCCMA has been working on the certification program for nearly three years, and recently published an extensive study guide and is preparing for the first certification examination next year (*P&I Age*, July 22).

NCCMA officials say they are aware of the criticism and plan to go ahead with the program. The association said its surveys show most cash managers support certification.

"Quite frankly, there's not a whole lot of concern (about certification) here," said James Wilson, cash manager at Blue Cross-Blue Shield of Indiana and president of the Central Indiana Cash Management Association.

Mr. Wilson said many cash managers believe certification is not necessary because most do not intend to make cash management a career, but plan to move up the corporate ladder. For example, he is the third cash manager at Blue Cross in 10 years.

He intends to take the certification exam because Blue Cross encourages professional development, but "there is not a strong interest in certification" by members of his association. Mr. Wilson said perhaps 15 to 20 of the 80 members might be interested.

James Wold, president of the Atlanta Treasury Management Association and cash manager at Oxford Industries Inc., is openly critical of the certification program.

"Our opinion is we don't see a need for it. I don't think 5% of our people will apply for it," he said. "We don't look at ourselves as being dead-ended in cash management but part of a bigger function . . . a part of the treasury function. We don't see cash management as an end in itself."

Mr. Wold said the certification program "seems a little misguided" and he does not intend to apply for the exam. He said the Atlanta association has discussed certification and "we found one or two who would like to take it."

"It is our opinion that the NCCMA ought not to spend much money on it," he said. "I predict a moderate turnout for the first exam. There will be some who will take it, mainly bankers and academics so they can hang a bunch of initials behind their name."

Certification "will die on the vine" after that, he said, and probably should not have been pursued as far as it has. The NCCMA started work on the program "and before anyone realized what was going on, it was way down the line," he said.

Mr. Wold said certification of cash managers is unnecessary because "it is not a complex body of knowledge. It's not that extensive. I don't think it's that big of a deal."

"Most cash managers are handling a lot of other things as well. It's not a full-time job in many cases," he said.

A similar attitude about certification is evident in the New Orleans Cash Management Association. Art Marr, immediate past president of the

Continued on page 28

Termination . . .

Continued from page 3

no company had made a move for UAL. The company plans to use the cash to help finance its recent acquisition of Pan American World Airways Inc.'s Pacific division for $750 million and 25 Boeings 737s from Frontier Airlines for $360 million. Around the same time, UAL bought Hertz Corp. from RCA Corp. for $587 million.

Although the company didn't disclose how it would finance the Hertz acquisition, analysts called the pension termination and reversion essential for financing UAL's expansion and thwarting any potential takeover (*Pensions & Investment Age*, June 24).

In takeover financing, "junk" bonds — debt securities below investment grade with high yields — make a much larger contribution in terms of absolute dollars and publicity.

Less celebrated, but growing in recognition, is the cash in overfunded pension plans, called "hidden assets" by Norman Weigner, senior vice president, Oppenheimer & Co., New York.

No one keeps track of pension terminations and acquisitions, potential takeovers or stock repurchases. But data on terminations from the PBGC and acquisitions by W.T. Grimm & Co., Chicago, indicate the use of surplus pension assets is increasing.

The accompanying chart lists some recent examples of the use of pension assets in corporate financing.

"It's definitely a gold mine to go after these overfunded plans," said Mr. Ibbotson.

"This is definitely one of the dangers of overfunding pension plans, especially when you consider the active takeover environment," he added. "It makes the pension plan attractive."

One of the most notable uses is the takeover of Great Atlantic & Pacific Tea Co. by the Tengelmann Group of West Germany.

It paid about $165 million for the supermarket chain; A&P's terminated pension plan generated a reversion of some $265 million, although the amount is still in dispute (*P&I Age*, May 27).

Occidental Petroleum Corp. took over Cities Service Co. for $4.1 billion. Occidental then terminated Cities Service's plans, recapturing $238 million, and its own plan, recapturing $136 million.

Mortimer Zuckerman bought U.S. News & World Report Inc. for $162 million. Its plan was terminated, bringing $18.7 million in surplus pension assets.

Lyon Metal's management is using the $12 million reversion from terminating the company's plan to help finance its $28 million buy-out to take the firm private.

Oppenheimer's Mr. Weigner said companies with overfunded pension plans appear to attract takeover speculation. He tracks the relationship of companies with overfunded pension plans and 13-D filings, Securities and Exchange Commission reports showing investor accumulations of shares.

"We found there is a correlation between 13-D filings and overfunding," Mr. Weigner said.

Mr. Ibbotson agreed that overfunding makes companies more attractive as takeover candidates. "It's a hidden asset," he said. "It doesn't show up on the balance sheet (only in footnotes of annual reports)."

A proposal by the Financial Accounting Standards Board would force corporations to put unfunded pension liabilities on their corporate balance sheets; but it appears it wouldn't accordingly list pension surpluses, keeping the assets "hidden."

"Raiders know how to find 'hidden' assets," Mr. Ibbotson said. "If it (pension overfunding) is on the balance sheet, raiders might have to pay a little more" for the company, because investors more likely would value the surplus in the stock price.

Mr. Ibbotson said one of the attractions of the overfunding is "how easy terminations can take place" to get at the money. In most cases, there are no proscriptions.

The use of pension plans as a source of corporate finance has its critics as well. Rep. Edward R. Roybal, D-Calif., chairman of the House Select Committee on Aging, has proposed legislation to stop the use of pension surpluses in many such takeovers, especially by companies using the reversion to help finance employee stock ownership plans to protect management and thwart takeovers.

But overfunded plans aren't always terminated for the reversion. Last year Malone & Hyde Inc., a $2.6 billion in sales retail distributor, was taken private by a management group and outside investors. Despite financing the buy-out with nearly 100% debt, or about $560 million, the company didn't terminate its plan, overfunded by 77%, with excess assets of $10 million. Randell Reiners, its manager of corporate finance, said a termination was suggested, although not pursued.

Other companies recapture pension surpluses before selling off a unit.

American Express Co., New York, has announced plans to sell off to the public part of its wholly owned Fireman's Fund Insurance Co., Novato, Calif. Earlier this year, American Express terminated the Fireman's plan, recapturing $120 million. A month later, American Express terminated its own plan as well, recapturing $90 million.

Ogden Corp. plans to sell off its shipyard and industrial products business for $375 million to an employee stock ownership plan. Some $80 million of the financing will come from a termination reversion.

But terminations of the acquisition's pension plan in a takeover appear more common; and more such terminations are likely. Chesebrough-Pond's Inc., which acquired Stauffer Chemical Co. for $1.218 billion, is considering terminating the Stauffer fund to recapture an estimated $100 million (*P&I Age*, July 8).

The termination of Central Soya Inc.'s plan to recapture about $40 million also is being considered. It was acquired by Shamrock Holding Co. for $325 million (*P&I Age*, June 24).

Reversions are being put to other uses as well. Celanese Corp. terminated its plan, recapturing $370 million, one of the largest such reversions, to bolster its corporate coffers.

Firestone Tire & Rubber Co. terminated its plan, recapturing $267 million. It is conducting a large stock repurchase program; so far, it has bought back 30% of its shares outstanding, spending $270 million.

Among other terminations already filed, Wilson Foods Inc., a potential takeover target, recaptured $42 million to help finance a reorganization.

Amerace Inc., acquired for $121 million in a management buy-out, is terminating its plan to get a $16 million surplus.

Mobil Corp., which acquired Superior Oil Co. for $10.1 billion, terminated the target's pension plans for a $29 million reversion.

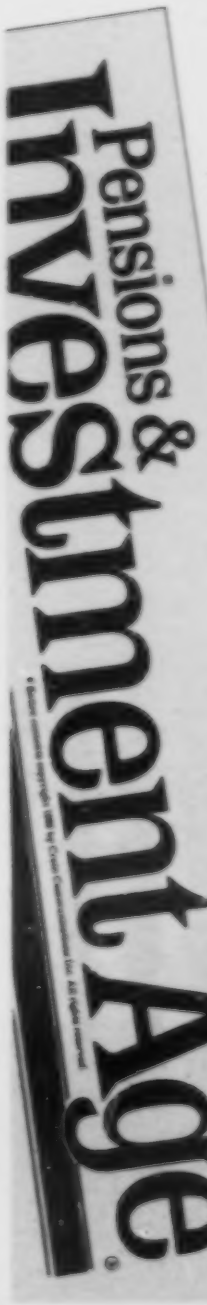
Jonathan Logan Inc. was acquired for $170 million by United Merchants & Manufacturers Inc. Its pension plan then was terminated for a $5 million reversion.

St. Regis Corp., acquired by Champion International Corp. for $1.8 billion, terminated its plan, with $88 million in surplus pension assets.

Sir James Goldsmith's company, Generale Occidental S.A. acquired Diamond International Inc. for $584.8 million; Diamond's terminated plan, generated a $12 million reversion.

Purex Industries Inc., taken private for $357 million, terminated its plan for a $12 million reversion. ■

26 important investment issues you should know about in the days and months ahead.



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Teachers target passive strategy

By Steve Hemmerick

SACRAMENTO, Calif. — The $14.5 billion California State Teachers' Retirement System will switch from mostly active to 50% to 67% passive management over the next three years, said Tom Flanigan, chief investment officer.

In addition, as part of the current preparation for long-term growth:

• A large, but yet-undetermined, amount will be brought in-house. All assets now are managed by external managers.

• About $2.6 billion will be moved to equities from fixed income to bring the equity allocation to about 40% from the current 22%.

While the changes involve a massive amount of money, they do not represent as big a philosophical change as it might first appear, said Mr. Flanigan. He was hired in May at $130,000 a year from his post as deputy chief investment officer for the New York State Common Fund.

Mr. Flanigan said the restructuring will be done for projected long-range growth to the year 2000.

With passive management, average risk-adjusted market performance is sought; with active management, better-than-average performance is sought, and performance usually is matched against a benchmark index.

He said the move to passive management isn't based so much on the usual interpretation of the efficient market theory, but rather because California and New York public funds will "be the market." The California Teachers could grow to

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Claim United violated law

Pilots fight termination

By Chuck Paustian

CHICAGO — The Air Line Pilots Association and five of its members have filed suit to prevent the planned spinoff/termination of the United Air Lines Inc. Pilots Retirement Income Plan.

The suit, filed late last month in U.S. District Court in Chicago, named United Air Lines Inc., Chicago, three plan fiduciaries — John M. Batten, D.O. Danis and John L. Cowan — and the Pension Benefit Guaranty Corp., Washington, as defendants.

The retirement income plan is composed of the United Air Lines Inc. Pilot Fixed Benefit Retirement Income Plan ("A Plan") and the United Air Lines Inc. Pilots Directed Account Retirement Income Plan ("B Plan").

The petition was filed by the pilots' union and Roger Hall, James Engelman and Thomas Sashko, all pilots employed by United and who serve on the ALPA Master Executive Council for the United pilot group as chairman, vice chairman and secretary/treasurer, respectively. J.V. Healy and B.K. Watkins, both retired United pilots, also were named as plaintiffs.

Robert A. Doughty, a United spokesman, said the company does not want to make any statement at this time because of the lawsuit.

The suit alleged United officials violated provisions of the Railway Labor Act and the Employee Retirement Income Security Act in their efforts to carry out the spinoff/termination and recover an estimated $511 million in excess assets.

It also charged the PBGC improperly promulgated the guidelines under which the spinoff/termination had occurred.

On June 10, United Air Lines announced it intended to spin off and terminate six of its defined benefit plans and recapture about $962 million in surplus assets (*Pensions & Investment Age*, June 24).

Michael E. Abram, an attorney with the law firm of Cohen, Weiss and Simon, New York, one of the firms representing the plaintiffs, said the actions taken by United officials violated provisions of the Railway Labor Act governing the amendment of RLA agreements.

"The Railway Labor Act says you can't make any unilateral changes in rates of pay," which includes deferred compensation, Mr. Abram said.

The suit said the United Air Lines board of directors, without prior notice, adopted a resolution June 7, providing for the reversion of excess assets from six of its defined benefit plans, including the pilots' fixed, or A plan. The adoption was subject to approval of the executive committee of the board of directors of UAL Inc., United's parent company.

According to the petition, the pilots' group charged United "deliberately and knowingly misled ALPA and active and retired participants" by not mentioning during negotiations to end the pilots' strike earlier this summer its intention to recover the excess assets from the pilots' plan.

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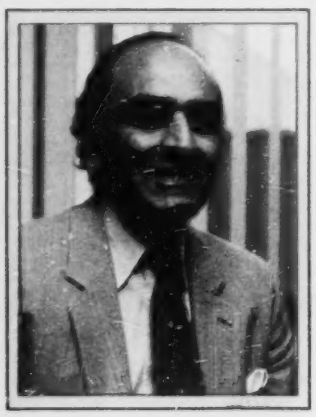
A mix of luck, wisdom

World Bank doubles profits

By Richard J. Gillespie

WASHINGTON — The treasury staff at the World Bank is acutely aware that any mistake could have an unconscionable impact on the lives of some of the world's poor, said Moeen Qureshi, senior vice president for finance.

Fortunately for these masses, the World Bank just reported a banner year, one in which the bank — mistakenly considered by some to be a charitable institution — turned in a profit of $1.14 billion for the fiscal year ended June 30, almost doubling the previous year's $600 million profit.



Moeen Qureshi

The investment management team, which produced a 12.63% realized return on the bank's now $17.4 billion portfolio, and realized and unrealized gains of 16.15%, contributed to the bank's stellar year.

These figures were achieved despite restrictions that the bank portfolio must be invested in 29 different currencies and is limited to fixed-income instruments with maturities of no more than five years and three months.

While the bank's investment allocations and restrictions make comparisons with standard benchmarks difficult, one measure of success is its realized liquidity spread — the difference between its cost of funds and its earnings on investments.

Eugene Rotberg, vice president and treasurer of the bank, said the 12.63% realized return contributed about one-third of the bank's profits, and helped boost the bank's realized liquidity spread — the difference between its cost of funds and its earnings on investments — to 3.96%.

As a direct result of its trading profits, the bank was able to reduce the interest rate it charged to less developed countries, Mr. Qureshi said.

A tea worker in Sri Lanka, which is a World Bank client.

"The way the bank is run as a financial institution is that short-term debt is passed through to the (less-developed countries), so if we make wise decisions, they get lower borrowing costs and if we borrow

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Kaman reshuffles, selects 2, trustee

By Alan Krauss

BLOOMFIELD, Conn. — The $90 million Kaman Corp. pension fund has completed a restructuring, hiring its first master trustee and two new investment managers, reshuffling accounts with three other money managers and creating an in-house market index to assess manager performance.

The restructuring, which took effect April 1, resulted from a portfolio evaluation undertaken for Kaman's pension administrative committee by SEI-Funds Evaluation, said to Russell Jones, a Kaman assistant vice president.

Kaman is a diversified defense contractor and distributor of industrial supplies and musical merchandise, with sales of about $550 million last year.

Following the study, Kaman allocated about $5 million each in balanced accounts to Fred Alger Management Inc., New York, and Thompson, Siegel & Walmsley, Richmond, Va.

The new allocations were funded by reducing balanced accounts with Connecticut National Bank, Hartford, to $25 million from $27 million, and with NCNB National Bank, Charlotte, N.C., to $15 million from $16.5 million.

Further, the fund reduced its allocation to CIGNA Corp., Hartford, to $19 million from $24.7 million, leaving $14 million in annuities and establishing a new, $5 million balanced account. A $2 million account was left with Aetna Life & Casualty Co., Hartford.

The fund named as its master trustee The Connecticut Bank and Trust Co., Hartford, Mr. Jones said. The master trust covers the fund's investments with Fred Alger and Thompson, Siegel & Walmsley, as well as an $11 million position in Kaman Corp. equities (held since before the Employee Retirement Income Security Act mandated a 10% ceiling on company stock) and

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Late news

U S WEST appoints

ENGLEWOOD, Colo. — U S WEST Inc.'s $5 billion pension fund has allocated $100 million to Brignoli, Curley & Roberts Associates, New York, for a computer-driven, quantitative equity account, said James R. Belquist, U S WEST's manager-trust investment management.

"The firm uses a mathematical approach with a strategy that emphasizes capturing value from the natural price volatility of stocks," Mr. Belquist said.

He declined to specify the source of the funds allocated to Brignoli, Curley.

GNMA date changes

NEW YORK — The Public Se-

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PIPER July indexes

	Latest mo.	Year to-date	Trailing 12 mos.
S&P 500	–0.13	17.09	32.53
OTC Inds.	2.28	19.19	21.35
Ryan Index*	–0.58	11.24	24.89
SLAE Gov't./Corp.*	–0.32	10.20	23.11

Source: Rogers, Casey and Barksdale Inc.
*Fixed income.

Wheeling-Pittsburgh can't pay

Contribution waiver sought

By Trudy Ring

PITTSBURGH — Wheeling-Pittsburgh Steel Corp. has asked the Internal Revenue Service to waive a $5.7 million pension fund contribution that was due July 31, company and union officials said.

The contribution was required as a condition of a 1983 funding waiver the IRS granted Wheeling-Pittsburgh. The company was to begin making monthly payments in July of the amount paid to beneficiaries two months before, said Howard Kline, counsel for employee benefits for the United Steelworkers of America.

George Raynovich Jr., Wheeling-Pittsburgh's general counsel, confirmed the company requested the waiver. He said Wheeling-Pittsburgh made the request because of the company's general financial condition, including "the fact that we're on strike and our cash is draining away."

The Steelworkers went on strike against Wheeling-Pittsburgh July 21 after bargaining teams failed to agree on terms of a contract to replace one nullified by a federal bankruptcy court. The company has sought protection from creditors under Chapter 11 of the Bankruptcy Code.

Mr. Raynovich said he didn't know when the IRS might make a decision on the waiver. IRS officials could not be reached for comment by press time.

A Pension Benefit Guaranty Corp. spokesman said the waiver request is the sole province of the IRS, but the PBGC is monitoring the situation carefully.

There has been speculation that Wheeling-Pittsburgh might terminate its pension plans, with unfunded liabilities estimated between $200 million and $350 million. However, Mr. Kline said the Steelworkers union was assured early this month that Wheeling-Pittsburgh has no intention of terminating the plans and that the board of directors has not authorized the company to do so. ■

Hedging is great for Gates

By Barry B. Burr

DENVER — Using stock index futures as a hedge, Gates Corp. said its more than $110 million in equity portfolios will never lose money.

Clayton M. Hill, director-corporate insurance and employee benefits, describes the strategy as similar to buying insurance to avoid losses.

With the strategy, "the downside risk is truncated; at the same time, the ability to capture market gains remains," said Larry D. Edwards, president of Leland O'Brien Rubinstein Associates Inc., Los Angeles.

Leland O'Brien Rubinstein has been using the strategy for Gates since March 1984.

The hedging strategy doesn't interfere with the stock holding or trading of Gates' four equity managers — Bankers Trust Co., New York; Thorndike Doran Paine & Lewis, Boston; Warburg Pincus Counsellors Inc., New York; and Wentworth Hauser and Violich Inc., San Francisco. Together, they manage about $110 million for Gates.

Leland O'Brien Rubinstein itself doesn't run any equity. It manages only the hedging strategy, trading stock-index futures.

"As it has turned out, it's been an inexpensive insurance policy for Gates, because we haven't had to put much of a hedge on," said Mr. Edwards.

So far, it has put on the hedge only twice for Gates, from May to July 1984 and then briefly again in October.

Since then, because of the general upward move of Gates' equity portfolio, Leland O'Brien Rubinstein hasn't had to hedge, Mr. Edwards said.

Leland O'Brien Rubinstein, partly owned by First Interstate Investment Services Inc., a unit of First Interstate Bancorp., Los Angeles, employs the strategy for about $1 billion of portfolios belonging to tax-exempt clients.

One of its largest clients, Manville Corp., also based in Denver, hedges its entire $560 million pension fund, fixed income as well as equities, with stock-index futures and fixed-income futures (*Pensions & Investment Age*, Aug. 6, 1984).

Gates has a hedging program for its fixed-income assets under way

Continued on page 77

CIBA getting aggressive

By Alan Krauss

ARDSLEY, N.Y. — Investments by the $400 million CIBA-Geigy Corp. pension fund may become "slightly more aggressive," with possible moves into international bonds and equities, real estate equities, venture capital and leveraged buy-outs, company officials said.

Money for the new investments would come from about $68 million in maturing guaranteed investment contracts.

Pension fund executives are considering the changes as a result of a recently completed, wide-ranging asset allocation study, conducted by company officials and their actuarial consultant, Towers, Perrin, Forster & Crosby. The study was undertaken to determine options for reinvestment of funds in two maturing GICs containing a total of 17% of plan assets, said Bill McHugh, CIBA-Geigy manager, trust investments.

A decision whether fund executives will adopt all or part of the strategies outlined in the study is expected in September, Mr. McHugh said.

A $40 million GIC held with Metropolitan Life Insurance Co., New York, matured earlier this month, while a $28 million contract with Prudential Asset Management Co. Inc., Newark, N.J., will terminate early in 1986, Mr. McHugh said.

The study showed the plan to be in good shape. Mr. McHugh said the study found the plan's demographics closely in line with national averages in terms of employee age and length of service. The rate of growth of fund assets — 16.5% annually over the past 10 years including both return on investment and company contributions — is adequate, according to the study.

The plan is well funded both on a termination basis and on an ongoing basis, he said.

"We found that the status of the fund would permit adoption of a

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Late news

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curities Association has announced a change in the September "48-hour rule" notification date for GNMA securities.

The notification date for submission of pool information on delayed-delivery transactions on GNMA securities has been moved to Sept. 13 from Sept. 16.

For Sept. 13 only, the Public Securities Association will extend the notification time from 3 p.m. EST to 4 p.m. EST.

The information is critical to investors having any GNMA mortgage security transactions settling in September, whether outright buys or sells, or financing transactions such as repurchase agreements or reverse repurchase agreements.

Divestiture finished

The United Nations Joint Staff Pension Fund, New York, and the University of Massachusetts endowment fund, Amherst, have completed divestiture of South Africa-related securities, officials said.

The $4 billion U.N. fund initiated a policy against South Africa-related investments more than 10 years ago and had been gradually selling off stocks since then. The amount divested by the fund was not available.

The university, with $4 million in assets, sold $370,000 worth of stocks in four companies. The fund had been following the state's policy of not investing in any companies doing business in South Africa, but recently refined its definition of "doing business," leading to the sales, a spokesman said.

Subsidiary formed

HARTFORD, Conn. — Connecticut Mutual Life Insurance Co. is creating CM Capital Advisors, a subsidiary of the firm's pension division, to advise pension funds in the $1 million to $10 million range on asset mix and allocation, said Gary Lineberry, second vice president pension division.

The insurer manages about $7 billion in commingled equity, fixed-income and real estate accounts for pension funds, he said.

Late money movers

• HARRISBURG, Pa. — The $8.1 billion Pennsylvania Public School Employees' Retirement System has committed $20 million to a new venture capital partnership with Century IV, Philadelphia.

• WHITE PLAINS, N.Y. — The $800 million Financial Institutions Retirement Fund has switched from using two custodial banks — Brown Brothers Harriman & Co. and Boston Safe Deposit & Trust Co. — to one, Bank of New York.

• NEW BRUNSWICK, N.J. — The $535 million Johnson & Johnson pension fund hired four equity managers, according to H. Scott Snead, manager-pension investments.

They are: Trinity Investment Management Corp., Boston, and First Manhattan Capital Management, Brignoli, Curley & Roberts Associates, and Dillon, Read Capital, all of New York. Mr. Snead declined to specify the allocated amounts.

The newly allocated funds came from excess assets previously carried in annuity contracts and new contributions, he said.

• TOPEKA, Kan. — The $130 million Kansas Power & Light Co. pension fund hired Renaissance Investment Management, Cincinnati, to run $23 million in equities, and New South Capital Management, Memphis, Tenn., to run $20 million in equities.

Renaissance replaces IDS Advisory Group, Minneapolis, and New South replaces Southeast Management Associates, the firm it split off from, a Kansas Power spokesman said. E.F. Hutton Consulting Services, Wilmington, Del., was consultant in the hirings.

• DETROIT — The $60 million Hudson-Webber Foundation, which makes charitable grants to Detroit-area civic and urban revitalization programs, has hired The Boston Co., Boston, to manage a $5 million aggressive asset-allocation account.

Funds will be invested in index funds mirroring the Standard & Poor's 500 stock index and the Shearson Lehman Government/Corporate bond index, as well as a money-market fund, according to Gilbert Hudson, president of the foundation.

• BALTIMORE, Md. — Crown Central Petroleum Corp. has completed a restructuring of its $39 million pension plan with the appointment of NCNB North Carolina to run a $500,000 real-estate equity account.

Earlier this year, the fund dropped the Travelers Investment Management Co. of Hartford, Conn., from a $2 million equity account and removed $18 million from its account with Union Trust Co. of Maryland.

The plan used the proceeds to fund two new equity managers to produce a more aggressive investment stance, according to P.J. Del Bene, corporate manager-administration.

After consultations with Hewitt Associates, the trustees awarded Northern Capital Management Inc., Madison, Wis., an $18 million account for a value-management approach in January, he said.

Lieber & Co., Harrison, N.Y., received a $6 million account at that time for small-cap value investing.

• WATERBURY, Conn. — Timex Inc. has chosen IDS Trust Co., Minneapolis, as record keeper for its pension plan and 401(k) plan, a Timex spokesman said.

Report footnotes give boot to FASB's rules

By Barry B. Burr
and Rick Rosenfeld

Companies with overfunded pension plans are becoming openly more critical about the Financial Accounting Standards Board's reporting procedure, complaining it exaggerates the amount of surplus assets.

An increasing number of the companies are criticizing the FASB in the pension footnotes of their 1984 annual reports, saying the required accounting procedure gives a misleading picture.

Though they don't say so in the reports, they privately expressed concern the reported overfunding might appear to be a wasted use of corporate money by overcautious pension officials or a temptation for corporate raiders looking for surplus cash to help finance a takeover. The companies contend, however, overfunding is a prudent way to finance projected benefit accruals.

Disagreeing with the FASB on pension (or any other) accounting isn't new. In the past, though, pension-related dissension has focused on reporting unfunded liabilities, rather than overfunding.

(The FASB has proposed companies place unfunded liabilities on their corporate balance sheets.)

Now, the FASB is encountering criticism from companies with overfunded plans. Most companies still report the footnote only as required by FASB. But an increasing minority complain the procedure shows a pension plan's status on a termination basis, rather than an ongoing basis, projecting work service and salary increases.

"Nothing FASB is currently looking at would change a thing," said Bruce Langton, assistant treasurer, International Business Machines Corp., Stamford, Conn.

While some companies complain the FASB procedure is misleading, others find the accounting board's numbers are very real; they increasingly are terminating the plans to recapture the excess assets.

Surplus pension assets among the 100 largest industrial and manufacturing companies as ranked by sales grew more than 210% in 1984 from 1983.

According to data on the Fortune 100 companies compiled by Wright Investors Service, Bridgeport, Conn.:

• Eighty-eight plans reported overfunding, or assets exceeding vested liabilities, in 1984, up from 85 plans the previous year.

• The 88 plans reported surplus assets of $39.2 billion in 1984, more than triple the $12.6 billion surplus reported by the 85 plans in 1983.

(The totals exclude American Telephone & Telegraph Co., which also had a surplus of $7.5 billion in 1984 and $22.4 billion in 1983; its figures skew the aggregate data due to the divestiture.)

Pension fund asset and liability data is on pages 44 and 45.

In accordance with FASB Statement 36, companies are required to report in a footnote in their annual report the present value of accrued benefits.

Because the figures are recorded next to the assets available for benefits, many company executives believe the plan's actual funding status may be misinterpreted as grossly overfunded on a termination basis, though the plan is on an ongoing basis.

As a result, many companies issued qualifying statements or a second set of funding figures to contrast the FASB data in their 1984 annual reports.

• General Electric Co.'s report stated its calculations "are more realistic (than the FASB calculations) because the benefit amounts include the expected future compensation and service."

Using the FASB methods, General Electric, Stamford, Conn., showed an overfunding of almost $3 billion with accrued vested and nonvested benefits of $9 billion and assets of $11.7 billion in 1984. By recognizing projected future salaries in its calculations, GE's overfunding turned into a $1.4 billion underfunding, with accumulated benefits of $11.1 billion.

For a number of years, the GE annual report has pointed out the discrepency between its own caluculations, taking into account future salary increases, and the FASB calculations.

Bernard R. Doyle, GE's manager of corporate accounting services, said his company publishes the second set of numbers to contrast the FASB data because of a philosophy that the annual report should be "as forthright and clear as possible."

"We are not particularly enamored of FASB 36," he said. "It's kind of off-point. They're saying compare pension obligation numbers and asset numbers that don't relate to each other."

• R.J. Reynolds Industries Inc., Winston-Salem, N.C., report's projection of future salary increases turned what was an overfunded plan using the FASB formula into a slightly underfunded one.

Using the FASB calculations, the company reported vested and nonvested liabilities of $914 million and assets of $1.18 billion last year. With allowances for salary increases, the level of liabilities reached $1.24 billion.

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Termination not part of restructuring

Manville pension plan untouched

By Fred Williams

Manville Corp.'s $600 million in pension assets apparently escaped unscathed from the company's proposed restructuring to allow it to emerge from bankruptcy.

But institutional shareholders of Manville stock, which likely would be severely diluted, aren't sure how they will fare.

The restructuring proposal involves the establishment of a $2.5 billion trust fund to fund claims arising from asbestos-related lawsuits against the company, a major producer of asbestos.

Speculation at one time focused on the Manville pension funds as a potential source of cash for the claim fund (*Pensions & Investment Age*, May 30, 1983) and more recently for the trust fund as the agreement was being developed.

J.L. Neill, director of trusteed benefit plans at Manville, said there are no plans to terminate the pension funds and use the surplus assets for that purpose.

"To the best of my knowledge, (the reorganization) should have no impact on the pension plans," he said.

"I haven't been asked to look into it (termination of the company's pension plans)," Mr. Neill said. "Termination was discussed in 1983 when the creditors committee had become aware of the fact the plans were well funded.

"We looked at it very carefully and we concluded it was not in the best interests of our employees. We told them (creditors) that we would revise our actuarial interest rate assumptions and funding methods and would look at a hedging program," he said.

Manville has two salaried pension plans and four hourly plans. The interest rate assumptions were adjusted from 6.5% on all plans to 8% for the hourly and 9% for the salaried plans, he said, effectively reducing the company's annual pension contributions. A hedging program was implemented in 1984 (*P&I Age*, Aug. 6, 1984).

"The overfunding will disappear over time since the company has reduced its annual contributions. The pension fund is not a vehicle for the reorganization effort," another Manville spokesman said.

The proposal to bring Manville out of bankruptcy would cut up to 80% from the value of Manville common stock, and financial analysts claim the plan faces a long and bumpy approval process.

Under terms of the proposal, which has been approved by the Manville board and attorneys representing future asbestos claimants, the trust would be funded by $815 million in cash and receivables and 50% of Manville's outstanding common stock, with the potential for an 80% dilution if necessary.

The $815 million will come from $315 million in insurance claims already settled, $300 million in cash from yet to be completed insurance

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Euroyen attraction returns

By Marci Baker

High-quality U.S. issuers have returned to the Euroyen marketplace after a six-month hiatus, this time in dual-currency transactions that are providing a savings of as much as 45 basis points below comparable domestic debt securities.

So far, six domestic issuers — the Federal National Mortgage Association, Honeywell Inc., Phibro-Salomon Inc. and the credit subsidiaries of American Express Co., IBM Corp. and Ford Motor Co. — have announced yen-based dual currency deals.

Together they will raise more than $700 million in the Euroyen arena. Another $500 million in dual-currency transactions is being raised by a number of foreign issuers.

"The deals are offering very cheap financing," noted one investment banker. "For the issuer, they are clearly superior deals." For that reason, investment bankers expect other deals before the market becomes fully saturated.

Corporate finance

"Dual currency" refers to foreign-denominated securities whose interest is payable in the issuing currency and principal is payable in dollars. The bulk of the Euroyen transactions have been 10-year, 25 billion yen offerings carrying 8% coupons. Euroyen deals involve yen-denominated bonds issued in Europe.

The deals include "a built-in cushion" for investors against depreciation of the dollar, said David Boyle, assistant vice president at Nomura Securities International, New York. The dollar-based principal on the issues will be redeemed at a fixed exchanged rate of 208 yen to the dollar, or just more than $120 million for a 25 billion yen issue. The actual exchange rate now is about 238 to 240 yen to the dollar.

Issuers are saving on financing costs largely through changing their yen-based obligations into fixed-dollar ones. Yen-denominated proceeds are converted to dollars, based on a preset exchange rate, when the deal closes. The cur-

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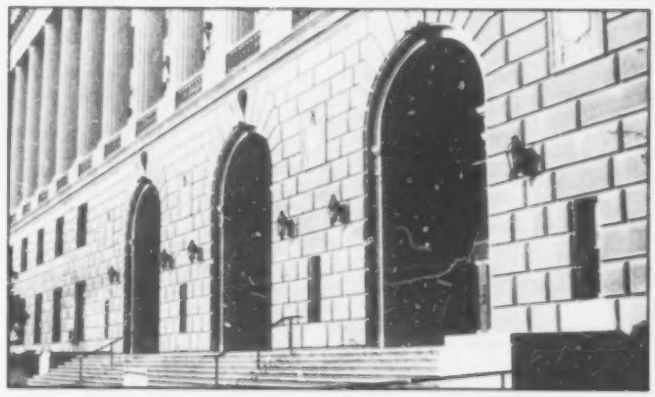

New annuity draws inspection by IRS

By Barry B. Burr

The Internal Revenue Service is holding up approval of pension plan terminations using so-called participating annuities, even though the Pension Benefit Guaranty Corp. has consented to the use of the new contracts.

Participating annuities differ radically from conventional annuity contracts sold by insurance companies to terminating pension plans.

In a participating contract, the company terminating its plan pays more initially to buy pension guarantees for beneficiaries than it would for conventional annuities. In turn, the company shares, or participates, in profits from favorable actuarial experience and investment performance in connection with annuities.

The new type of contract makes offering annuities appealing to more insurance companies, inducing bidding competition. The contracts, depending on how they are written, allow for banks and independent investment counselors to continue managing money after a termination. With conventional annuities, insurance companies automatically take over the money management.

So far, Firestone Tire & Rubber Co., Akron, Ohio, is the only known company to buy participating annuities, although an unidentified company also bought such contracts and Inco United States Inc., New York, among others, has been considering them for its terminated pension plan (*Pensions & Investment Age*, May 13).

Firestone and the unidentified company received PBGC approval to use participating annuities in their terminations.

Firestone bought a $397 million participating annuity contract from CIGNA Corp., Hartford, Conn., before the IRS issued its directive May 31.

The one-page IRS memorandum, which was sent to assistant regional commissioners, said, in part, "We are considering the effect upon plan qualification, if any, of using participating annuity contracts to provide benefits upon termination of an employee plan.

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